Supreme Court, U. S.
FILED
JAN 27 1978
MICHAEL RODAK, JR., CLERK

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1977

No. 77-918

THE FIRST NATIONAL BANK OF GLEN HEAD,
Petitioner,

v.

DONALD KATZ, Trustee in Bankruptcy of Oakland Foundry Company of Belleville, Illinois, Inc.,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF FOR RESPONDENT IN OPPOSITION

DAVID J. LETVIN
412 Missouri Avenue
East St. Louis, Illinois 62201
(618) 274-0434
Attorney for Respondent

JOEL A. KUNIN
COHN, CARR, KOREIN, KUNIN and BRENNAN
East St. Louis, Illinois
MURRAY S. LUBITZ
KAZLOW & KAZLOW
Scarsdale, New York
Of Counsel

St. Louis Law Printing Co., Inc., 812 Olive Street 63101 314-231-4477

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OPINIONS BELOW

The opinion of the Second Circuit, not yet officially reported, appears in Appendix I annexed to the petition. The opinion of the United States District Court for the Eastern District of New York, dated October 19, 1976, is officially reported at 424 F.Supp. 1174, and a copy thereof is annexed as Appendix II to the petition.[1]

[1] References to the opinions of the Court of Appeals and District Court opinions herein will be made by citation to the pagination of Petitioner's Appendices. (Pet. A. . . .)

JURISDICTION

The jurisdictional requisites are adequately set forth in the petition.

QUESTIONS PRESENTED

1. Whether a trustee in bankruptcy, seeking to set aside as a preference a bank's set-off of its bankrupt depositor's funds, who shows:

> (a) That a pre-bankruptcy build-up was made in a checking account that was opened and maintained as security for a loan from the bank to the depositor and not used for ordinary business purposes; and further shows
>
> (b) That the deposits constituting the build-up were neither made by the depositor nor accepted by the bank in the ordinary course of business; and further shows
>
> (c) That the bank had knowledge of the build-up, and of the depositor's financial difficulties and was in communication with the bankrupt immediately prior to set-off;

has produced sufficient evidence that the deposits were a transfer, and the bank a transferee under Section 60(a) of the bankruptcy act, to avoid summary judgment?

2. Whether the Second Circuit's alternative holding, that in determining whether the deposits were made in the ordinary course of business it is proper to review the ordinary course of the bankrupt depositor's business and his course of transactions with the bank, is consistent with prior holdings of this court?

3. Whether the Court of Appeals properly applied the law respecting summary judgment in reviewing the trustee's answering papers to the bank's motion for summary judgment?

STATUTES AND RULES INVOLVED

The pertinent statutes are set out in the Petition (Pet. 3-4).

STATEMENT OF THE CASE

The Petitioner Bank's statement of facts is "distilled from the opinions of the lower courts." (Petition p. 5). Had the bank looked to the record on appeal, however, it would have found substantial detailed evidence to sustain the findings of the Court of Appeals. The inadequacy of the fact statement provided by petitioner, as well as substantial misinterpretation by the bank of both the evidence and the holding of the Court of Appeals below, compel respondent, the trustee in bankruptcy, acting pursuant to Supreme Court Rule 24, to restate the evidence and course of proceedings below in detail in order to demonstrate the reasons why petitioner's petition for writ of certiorari should not be granted.

Respondent, Donald Katz, Trustee in Bankruptcy of Oakland Foundry Company of Belleville, Illinois, Inc., brought this action to set aside, as a voidable preference, a set off of $108,-783.91 from the bankrupt's account by the petitioner, First National Bank of Glen Head, pursuant to § 60 of the Bankruptcy Act, 11 U.S.C. § 96. It was the gravamen of the Complaint that $108,741.07 deposited by the Bankrupt into its previously inactive bank account during the 2½ months immediately preceding bankruptcy, was intended as a preferential payment of an outstanding indebtedness of the Bankrupt, which indebtedness was personally guaranteed and secured by the Bankrupt's President and owner, Herman Brede.

The District Court, in allowing petitioner Bank's Motion for Summary Judgment, assumed that at the time of the set off,

Oakland was insolvent and that the Bank had reasonable grounds to believe that Oakland was insolvent. The Court further recognized that the set-off was for the benefit of the creditor, was on account of an antecedent debt, was made within four months of bankruptcy, and enabled the Bank to obtain a greater percentage of its debt than other creditors of the same class. The Court held, however, that there was no transfer within the meaning of 11 U.S.C. § 96, since there was no evidence "to show any complicity by the Bank" in the bankrupt's president's scheme to make these funds available for a setoff in the event of impending bankruptcy.

The Court held that in determining whether the monies deposited in the Bank were built-up in the regular course of business, the proper test is only whether the deposits were accepted by the Bank in the regular course of its business. As the District Court stated:

> "The test is not whether the deposits were made in the depositor's regular course of business, but instead, whether they were accepted by the Bank in its regular course of business." (Pet A. 24-25)

Whether the deposits were made in the regular course of the Bankrupt's business, and whether they were made in the regular course of business between the Bank and the Bankrupt were held not relevant by the District Court.

The trustee appealed, contending (1) that the correct standard for determining whether the deposits were made in the ordinary course of business required inquiry into whether the deposits were made in the ordinary course of the bankrupt's business and in the ordinary course of transactions between the bankrupt and the bank; and (2) that no matter whose ordinary course of business is looked to, there was sufficient evidence in support of the trustee's case to go to trial, and it was therefore error to grant summary judgment against the trustee.

The Court of Appeals reversed. The panel was *unanimous* in concluding that the District Court erred in entering summary judgment. The entire panel agreed that even applying the District Court's "bank's only" ordinary course test, the trustee had presented sufficient evidence to allow the question whether there was a transfer within the meaning of § 60(b) of the Bankruptcy Act to go to trial.[2] And the majority of the panel, in an opinion by Judge Timbers, further concluded that

> "In view of the purpose of the inquiry, it does not make sense to consider only the bank's course of business. If the deposits somehow are out of the regular course of the depositor's business, the bank's normal procedures, or the usual course of the dealings between the depositor and the bank, then an inference can be drawn that the deposits were not ordinary deposits but served to transfer the depositor's property to the bank."

The entire court agreed to reversal and remand, and to the trustee's contention that its answering papers to the bank's motion for summary judgment had presented sufficient evidence to defeat the motion. The sole basis for difference of opinion within the court was the correct standard to be applied to the evidence at trial.

DETAILED FACTS BELOW

The facts from which the unanimous court concluded that summary judgment was improper all appear in the record, and are as follows:

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[2] The Court did not hold, as petitioner argues (Petition, p. 8) that the dopisits were transfers; the issue before the court was not whether a transfer had been made, but only whether the trustee had met his burden in responding to the bank's motion for summary judgment. Thus, the Court merely held that the trustee had shown enough evidence on the issue of whether there was a "transfer" to avoid summary judgment.

Oakland Foundry Company of Belleville, Illinois, Inc., the Bankrupt, was a wholly-owned subsidiary of Electronic Cabinets, Inc. All the stock of Electronic Cabinets, Inc., as well as all of the stock of H. W. Brede Co., Inc., was owned by Herman Brede and his wife, Betty, of Upper Brookville, New York. Brede was the President and Chief Executive Officer of Oakland Foundry.

Oakland maintained two checking accounts at the St. Clair National Bank of Belleville, Illinois, one checking account at the Trade Bank and Trust Company of New York (not pertinent to these issues), and one checking account at First National Bank of Glen Head, New York, which was opened on January 16, 1969.

The Loan Transaction

In consideration of a loan in the amount of $125,000.00, Oakland Foundry executed a Promissory Note in like amount in favor of First National Bank of Glen Head. This Note was executed on or about January 16, 1969, and matured on April 16, 1969. The Note was renewed quarterly until June 18, 1970, at which time Oakland's obligation was made payable on demand.

The Bank ordinarily required a personal Guarantee on corporate borrowings by small individually held corporations such as Oakland. In this instance, at the time the loan was made, Electronic Cabinets, Inc., Herman Brede and Betty Brede, each guaranteed Oakland's indebtedness to the bank. Without the personal guarantee of the Bredes, the Bank would not have made the $125,000.00 loan to Oakland.

Oakland's indebtedness to the Bank was further secured by a pledge to the Bank by the Bredes of all of the stock of Electronic Cabinets, Inc. and all of the stock of H. W. Brede Company, Inc.

On June 18, 1970, when Oakland's indebtedness was converted to a demand Note, as additional security on the loan, the Bredes gave the Bank a Second Mortgage on their Upper Brookville, New York, home.

On January 16, 1969, the same day that the Bank loaned Oakland $125,000.00, and pursuant to the Bank's usual practice, Oakland opened a general checking account with the Bank. The Bank did not pay interest on deposits in this account.

The Bank's Knowledge of Oakland's Financial Difficulties.

Before the Bank made the loan to Oakland, it was aware of the company's financial problems. It expressed concern that Oakland had turned only losses for the eleven months preceding the loan, and instead of loaning Oakland $250,000.00, as requested, loaned it only $125,000.00. The loan was made not on the strength of Oakland's capacity to repay it, but on Brede's individual financial strength apart from Oakland Foundry.

During the 2½ years following the loan and before Oakland's bankruptcy in July of 1971, the Bank continued its awareness of Oakland's financial straits. Anthony Famighetti, at all times here pertinent, the President of the First National Bank of Glen Head, testified that he knew that Oakland was having difficulties as early as 1970, and that he knew that Oakland had been operating for years on a continuing loss basis. Indeed, the reason the Bank required additional collateral from Oakland was because it knew that Oakland had not earned a profit during the several years prior to its 1971 bankruptcy. In June of 1970, at the time the second mortgage was taken on Brede's home, Oakland had an accumulated deficit of $300,000.00 and had lost $100,000.00 in the prior calendar year. The Bank's credit memo of June 18, 1970

reflects that even at that early date, the Bank advised Oakland that it "want[ed] out." In 1970, Famighetti was concerned about Oakland's cash flow, knew that Oakland owed $250,-000.00 to the Small Business Administration, and had total debts too heavy for it to carry. The Bank knew that Oakland had obtained loans to the legal limit in 1970, from the St. Clair National Bank in Belleville, Illinois where Oakland maintained two checking accounts and did most of its banking. The Bank also knew that Oakland was financing its receivables through a factoring organization. The Loan Committee of The First National Bank of Glen Head, in 1970, discussed Oakland's financial situation and its low working capital and knew of the low balance maintained in Oakland's Glen Head account. Famighetti admitted that the petitioner bank became aware of Oakland's "adverse financial condition" as its financial statements, which reflected the loss history, were received by the Bank. Additionally, Famighetti stated that he felt that Oakland was always in an adverse financial condition. He stated, specifically, that he was aware of Oakland's losses for the years 1968, 1969 and 1970.

The Bank had knowledge that Oakland gave false information in its Dun & Bradstreet Report for calendar 1970, the report representing sales of $1.4 million, and the income statement available to the Bank representing sales at only $546,000.00. The Dun & Bradstreet Report thus indicated sales in excess of 2.56 times the data available to the Bank.

In addition, Brede had been in close contact with the Bank respecting Oakland's obligation to the Bank during the few months immediately preceding the set-off, and the Bank had knowledge of Oakland's financial condition during those last few months as a result of discussions with Brede and one of Oakland's employees. In 1970, aware that the St. Clair National Bank and the Small Business Administration were creditors of Oakland, the Bank began asking that a substantial "compensating balance" be maintained in the Oakland checking account. The reason the Bank's President gave for making such a demand was "to be sure that we weren't left out in the cold, since we were extending substantial dollars, too."

The Ordinary Course of Business of Oakland and the First National Bank of Glen Head.

By March, 1971, Oakland had ceased normal, ordinary business operations.

Until February, 1971, Oakland regularly met its factory and office payrolls. In March, 1971, a much smaller factory payroll was met, and some back-payments were made on the factory payroll. In addition, a reduced office payroll was met that month. In April, 1971, no factory payroll whatsoever was reflected, and the reduced office payroll was met. By June, 1971, the office payroll was further reduced, and the factory payroll again was not evident.

Although the Bank has taken the position in this litigation that the checking account which Oakland maintained with it was a general business account, Famighetti testified that the Bank was not aware of what types of obligations the checks on the Glen Head account and the St. Clair account were used to pay. In fact, virtually all of the routine banking done by Oakland was done through its two accounts at St. Clair National Bank of Belleville.

The character of Oakland Foundry Company's "ordinary course" business transactions can best be understood by a study of activity in its main bank checking accounts. Two of these checking accounts were with St. Clair National Bank of Belleville, Illinois. One was the Foundry's regular account and the other was the Foundry's payroll account. The St. Clair Bank was located within one mile of Oakland Foundry's place of business. The third account was that with the petitioner, First

National Bank of Glen Head, New York, that was opened as a condition to the bank making the $125,000 loan.

A review of the transactions between Oakland and the First National Bank of Glen Head shows that from July of 1970, through March of 1971, a modest balance of between $1,300.00 and $5,800.00 was maintained in that account. Deposits were occasionally made, as were withdrawals, but by and large the account was inactive. In July 1970, no checks were drawn on this account. In August 1970, three checks were drawn. The records of September of 1970 through April of 1971, a period of eight months, reflect only minimal activity in the Glen Head account.[3]

The Build-Up.

The pattern changes markedly on or about April 20, 1971. During the next two weeks enough deposits were made in the Glen Head account to bring the balance from $865.09 to $68,603.65 by the end of April. In May of 1971, further deposits were made bringing the balance in the Glen Head account to $102,066.14. In June, eleven deposits were made in the Glen Head account bringing the balance therein to $109,348.66 according to records of Bankrupt. On the first of July,

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[3] From September, 1970, to April, 1971, the only transactions in the Glen Head account consisted of the following:

1. A check from the Glen Head account, payable to Glen Head on October 15, 1970;

2. A withdrawal of $300.00 on November 20, 1970;

3. A deposit of $3,000.00 on January 25, 1971, and a simultaneous withdrawal payable to First National Bank of Glen Head for interest of $2,656.25 on January 25, 1971;

4. A deposit of $2,922.79 on March 8, 1971; and on April 13, 1971, a check in the amount of $2,656.25, payable to Glen Head for interest; and

5. On April 15, 1971, a check to Dun & Bradstreet in the amount of $792.40.

After charging Oakland's account with those last two checks, the balance was a meager $865.09.

one final deposit was made into the Glen Head account, bringing the amount of money in the account (without considering the setoff by the Bank on June 30) to $109,597.16.

This final deposit was made *after* Brede's June 29 call to Famighetti in which Brede told Famighetti that Oakland was experiencing "complications" with its creditors. This final deposit was also made *after* Famighetti ordered that payment was not to be made on checks drawn on Oakland's account.

Thus from April 15, 1971, when the balance was $865.09, in a period of 2½ months, a total of $108,732.07 was placed in the account.[4] During that 2½ months, no withdrawals at all were made until the defendant set off the account in the amount of $108,783.91 on June 30.

Defendant argued below, and contends here, that this account, on which no checks at all were written for 2½ months, was a regular checking account used for everyday business purposes.

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[4] The deposits which constituted the build-up were as follows:

Date	Amount of Deposit
4/20/71	$ 2,546.63
4/21/71	2,071.00
4/26/71	43,120.93
4/28/71	20,000.00
5/04/71	4,681.76
5/07/71	668.81
5/18/71	21,451.01
5/25/71	1,303.47
5/28/71	5,357.44
6/01/71	484.94
6/05/71	1,588.68
6/07/71	688.83
6/09/71	982.05
6/14/71	898.68
6/10/71	9.70
6/21/71	820.17
6/25/71	1,157.50
6/29/71	88.22
6/22/71	19.00
6/30/71	564.75
7/01/71	248.50

From January 1, 1971 to July 15, 1971, a period of six and one-half months, only three checks were drawn on the First National Bank of Glen Head by Oakland, and two of these were to pay interest to Glen Head on the outstanding obligation of the Bankrupt.

Oakland's Ordinary Course of Banking With St. Clair National Bank.

One need only view the Bankrupt's regular bank account at the St. Clair National Bank of Belleville for the same period of time to see that virtually all of Oakland's routine business was processed through this account.[3] Between July, 1970 and May, 1971, the bankrupt made 112 deposits, and drew 891 checks. These checks were drawn for the purpose of paying payables, transfer funds for payroll to the payroll account, taxes, operating expenses and other items connected with the "ordinary" operation of Bankrupt's business.

The Set-Off.

First National Bank of Glen Head, of course, had full knowledge of the character of the acivity in Oakland's account with

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[3] A review of the bankrupt's banking records with the St. Clair National Bank shows the following transactions:

	Number of Checks	Number of Deposits
July, 1970	149	16
August, 1970	58	8
September, 1970	118	11
October, 1970	78	17
November, 1970	120	17
December, 1970	65	8
January, 1971	43	8
February, 1971	112	10
March, 1971	66	10
April, 1971	49	6
May, 1971	33	1
TOTAL	891	112

it. Famighetti admitted observing the build up himself, and the Bank knew how few withdrawals were being made on the account, knew the nature of at least some of those withdrawals, since most were to pay interest to the Bank itself, and knew that such was not the pattern of an ordinary business account.

On June 29, 1971, Brede called Famighetti to tell him that Oakland was in financial trouble, and that he was going to call his other creditors and try to work his way out. Famighetti immediately placed a freeze on Oakland's account, barring all withdrawals. The next day, on June 30, 1971, the petitioner, First National Bank of Glen Head, set off the sum of $108,783.91 and applied it against the outstanding loan balance of Oakland in the amount of $125,000.00.

Oakland Foundry was adjudicated a Bankrupt on August 18, 1971, pursuant to an "Involuntary" Petition which was filed against it on July 15, 1971, just two weeks after the Bank set off the funds in the account against Oakland's outstanding debt. Brede subsequently paid off the remainder of the obligation.

REASONS FOR DENYING THE WRIT

I

This Case Turns on Its Own Narrow Facts: the Court of Appeals Correctly Held That There Is a Fact Question Presented as to Whether the Deposits Were Made and Accepted in the Ordinary Course of Business, Thus Summary Judgment Was Improperly Entered.

The writ should be denied because the decision and disposition below are premised on the specific facts of this case, and do not present issues of general importance to bankruptcy jurisprudence. The Court of Appeals recognized that in determining whether Oakland and Glen Head had a traditional debtor-creditor relationship, or whether the bank, in accepting Oakland's deposits, received a transfer, the fact finder must determine whether the deposits were made in the ordinary course of business (Pet. A. 8). "A court must determine from *all the circumstances* whether the deposits were made in the regular course of business" in determining whether a set-off is a "transfer." (Pet. A. 9). Its conclusion that issues of fact are present which preclude summary judgment is a finding limited to the particular facts of this case.

Examination of "all the circumstances" surrounding the set-off shows that it is likely that these deposits were not made in the regular course of business. Summary judgment was thus improperly ordered by the District Court.

The account itself was not Oakland's ordinary business account, but was, instead, maintained as security for its loan from Glen Head.[6] The account was opened as a requirement to al-

[6] In *Citizens National Bank of Gastonia v. Lineberger*, 45 F.2d 522 (4th Cir., 1930), the court stated: "If there were showing that

lowance of the loan. When Glen Head learned that there were other substantial creditors in the picture, it demanded increased security in the form of compensating deposits which bore a relationship to the size of the loan.

The ordinary, daily business of Oakland was conducted not through its Glen Head account, but rather through its regular business account in the St. Clair National Bank of Belleville, Illinois. Between July, 1970 and May, 1971, Oakland made 112 deposits into its regular account there, and wrote 891 checks on the account. Those checks were drawn for the purpose of paying payables, taxes, ordinary operating expenses, and to transfer funds to the payroll account. The period between September, 1970 and April, 1971, immediately before the build-up, in the Glen Head account, was markedly less active. From January 1, 1971 to July 15, 1971, a period of six and one-half months, only three checks were drawn on the Glen Head Account, and two of those were to pay interest to Glen Head on Oakland's outstanding obligation.

The build-up was not made by Oakland in the regular course of its business. Indeed, by the time the Bankrupt began the build-up, it was virtually out of business. One month before the build-up began, in March, 1971, Oakland severely cut back its payroll; and the month it commenced the build-up, April, 1971, the factory had ceased to be a going concern and the office staff had been cut back. The next month, a second round of cut backs was made in the office payroll, the factory having ceased operations the previous month. Bank deposits made after a factory or business has ceased its operations are not made

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the deposits in question were made fraudulently or collusively, as a cloak for payments to the bank or as a means of giving it security, the trustee could avoid them under the Bankruptcy Act, without resort to the trust fund doctrine, if the bank were shown to have been a party *to the fraud or collusion, or to have accepted the deposits as a means of obtaining payment or security.*"

in the regular or ordinary course of business. *Merrimack National Bank v. Bailey*, 289 F. 468 (1st Cir., 1923); cert. denied 263 U.S. 704; *Cardozo v. Brooklyn Trust Co.*, 288 F. 333 (2d Cir., 1915); *Gates v. National Bank of Richmond*, 1 F. 2d 820 (D.C. Va., 1924); *Wilson v. Nebraska State Bank*, 126 Neb. 168; 252 N.W. 921, 24 Am. Bankr. Rep. N.S. 621 (1934) (Pet. A. 11).

Furthermore, Oakland instituted the build-up with the Glen Head Bank to protect Brede, since Brede had personally guaranteed the obligation, had pledged all the stock in his several companies to the bank as security on Oakland's loan, and since Brede had further mortgaged his home to the Bank to secure the loan. Even the District Court recognized that this was the reason the deposits were made (Pet. A. 24). Protection of a corporate officer's private finances is by no means a practice recognized as being one done in the ordinary course of business.

Nor was it the ordinary course of Oakland's business to make such large deposits in its New York account over such a short period of time, without making any withdrawals. Oakland deposited $108,732.07 in two and one-half months without writing a single check on the account. The bank paid no interest on deposits in this account. Examination of Oakland's prior banking practices reveals this to have been a highly unusual sequence of acts.

The trier of fact could easily conclude that the bank did not accept these deposits in the ordinary course of business. The account was maintained as security for the $125,000.00 loan. Knowing about Oakland's other creditors, including the Small Business Administration and the St. Clair National Bank, petitioner Glen Head asked, in 1970, that a substantial "compensating balance" be maintained in the account. The bank's president gave his reason for demanding this compensating balance:

> "to be sure that we weren't left out in the cold since we were extending substantial dollars, too."

Brede had been in close contact with the bank during the months immediately prior to the set-off. Conversations between the bank and both Brede and one of Oakland's employees had informed the bank of Oakland's worsening financial condition during those last few months.

Even before the loan was made, the bank knew of Oakland's financial problems. It loaned Oakland only half the amount it had requested, since Oakland had turned only losses during the eleven months prior to obtaining the loan, and made the loan not on Oakland's financial strength, but on Brede's. When the bank demanded additional collateral on the loan, it did so because of Oakland's continued inability to earn a profit. In June, 1970, the bank advised Oakland that it "want[ed] out." The bank's entire loan committee discussed Oakland's bleak financial picture, and the bank learned of Oakland's "adverse financial condition" as it received Oakland's periodic financial statements. The petitioner bank knew in early 1971 that Oakland had falsified its 1970 Dun & Bradstreet report.

A set-off made by a bank on its depositors' account which is made after the bank has stopped withdrawals on the account is not a transaction made in the ordinary course of business. *Mechanics & Metals National Bank v. Ernst*, 231 U.S. 60 (1913); *Irving Trust Co. v. Bank of America National Association*, 68 F. 2d 887, 890 (2d Cir., 1934). Here, the bank froze Oakland's account on June 29, 1971, immediately following Brede's phone call to Famighetti telling him that Oakland was in financial trouble, and that he was calling his other creditors in an attempt to work his way out. The very next day, the bank made the disputed set-off.

These facts show that the set-off and Glen Head's acceptance of the deposits were not necessarily made in the ordinary course of business. The Second Circuit recognized that many factual issues were present, noting that this record presents "such critical issues of fact as whether, in view of the build-up

and real nature of the Glen Head account, the bank acted in good faith in accepting the deposits", "whether the account in fact was a general deposit account," (Pet. A.3) and "whether the bank was aware of Oakland's intentional build-up of its account as reflected in the bank's acceptance of the deposits other than in the bank's regular course of business." (Pet A. 5). Proof of "Famighetti's continuous knowledge of the course of Oakland's accelerating financial difficulties and his communications with Brede," (Pet. A.7) held the court, would prove the bank's acceptance of these deposits outside its ordinary course of business. It was "to resolve these and other issues of fact"[7] that the court unanimously reversed and remanded.

Whether a normal debtor-creditor relationship was present was a factual question, not appropriate for disposition by summary judgment. Here the Trustee, in response to the Motion for Summary Judgment made by the bank, produced evidence that a unanimous panel of the Court of Appeals held would allow a conclusion that these deposits were neither made nor accepted in the ordinary course of business.

In summary, the Court of Appeals' holding was limited to the specific facts before it. The review of this decision by the United States Supreme Court would occasion no opportunity to consider any issue of general importance to bankruptcy jurisprudence. The petition for a writ of certiorari should therefore be denied.

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[7] The jury could well conclude on this record that the bank, in light of the extensive and detailed knowledge it had of the bankrupt's adverse financial circumstances, would not have allowed any withdrawals from this account during those final days. And even if it were to be concluded that these withdrawals would have been permitted, allowance of such withdrawals would not, alone, make mandatory a finding that there were no transfers. As the Court of Appeals below correctly recognized quoting *Merrimack National Bank v. Bailey*, 289 F. 468, 470 (1st Cir.), cert. denied 263 U.S. 704 (1923): "The fact that such bank creditors may honor checks on deposit does not control. In this case, checks to cover these deposits were not drawn and paid." (Pet. A. 8-9, n. 7).

II

The Majority's Decision Below Is Consistent With the Prior Holdings of This and Other Courts.

The Second Circuit majority, in its alternative holding, correctly recognized that a bank's set-off may be attacked as a voidable preference if the bankrupt deposited the funds in question other than in the ordinary course of its business, intending a transfer, and the bank had reasons to know, at the time the deposits were made, that the depositor was insolvent.

No case has held the regular course of business requirement to be applicable solely to the bank and no case has required that in order for a build-up followed by a set-off to constitute a transfer, the bank be an active participant in the build-up. A showing of a transfer within the meaning of the Act is made where the bankrupt's intention is to effect a preference, where, as here, at the time the deposits were made, the bank knew of the depositor's insolvency.[8]

The bank's argument that "a depository bank must be culpable in order for it to be held liable as the recipient of a preferential transfer" (Petition, p. 15) is an improper statement of the law. The Court of Appeals below correctly recognized that "a bank's participation in the build-up . . . is not a prerequisite to a finding that there has been a transfer." Rather, the intent of either the depositor or the bank to effect a transfer is sufficient to allow the conclusion that a transfer has been made. As the Court stated in *Cusick v. Second National Bank*,

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[8] There is no issue presented to this court respecting Oakland's insolvency. The trial court assumed Oakland was insolvent at the pertinent time and that the bank had reasonable grounds to so know (Pet. A. 21); the Court of Appeals recognized that "whether the bank had reasonable cause to believe that Oakland was insolvent is something that the trustee must prove at trial and is a question for the jury." (Pet. A. 13, n. 10).

73 App. D.C. 16, 115 F.2d 150 (1940), a deposit may be a preferential transfer if "either the [depositor] or the Bank, at the time of the deposits, intended them to operate as a payment of the notes," and that a deposit would not be a preferential transfer only "if both depositor and the bank intend" that it would be subject to withdrawal. In *Mayo v. Pioneer Bank & Trust Co.*, 270 F.2d 823 (5th Cir., 1969), the Court agreed, noting that the trustee could attack a set-off as a preference if "at the time of the deposits either the company or the bank intended them to operate as payment of the debt rather than as an ordinary deposit subject to the depositor's withdrawal."

The Court of Appeals below focused on the problem quite clearly, recognizing that the scope of inquiry must be consistent with the reasons for disallowance of set-offs in non-ordinary course transactions:

> "In deciding whether a bank's set-off is a 'transfer', a court must determine from all the circumstances whether the deposits were made in the regular course of business. In view of the purpose of the inquiry, it does not make sense to consider only the bank's course of business. If the deposits somehow are out of the regular course of the depositor's business, the bank's normal procedures or the usual course of dealings between the depositor and the bank, then an inference can be drawn that the deposits were not ordinary deposits but served to transfer the depositor's property to the bank. By limiting its inquiry to the regular course of the bank's business, the district court below failed to take into account that 'a deposit may be made the cloak for some other transaction, such as payment or the giving of security; and in such case equity, which looks through form to substance, will treat the transaction according to its real nature.' Citizens' National Bank of Gastonia v. Lineberger, supra, 45 F.2d at 527-28." (Pet. A. 9)

This Court recognized, in the leading case of *Studley v. Boylston National Bank*, 229 U.S. 523, 527 (1913), that the intention of a depositor alone to effect a preference is sufficient to allow a finding of transfer:

> "We find nothing in the record to indicate that the deposits were made for the purpose of enabling the bank to secure a preference by the exercise of the right of set-off. The case, therefore, comes directly within the decision in *New York County National Bank v. Massey*, 192 U.S. 138."

Thus, this Court recognized that *Massey* controls only in those cases where there is no evidence of record to indicate that the purpose of the depositors in making the deposits was to secure a preference, and spoke strictly of purpose of making deposits. No mention was made of purpose in accepting funds for deposit.[9] And this record is replete with facts showing Oakland's intent summarized in Section I above. Certainly a sufficient showing of the depositors intent to effect a preference was made to avoid summary judgment. Indeed, even the District Court recognized: "I have assumed that the deposits were not made by Oakland in the ordinary course of its business, but were instead made . . . to place funds within easy reach of the bank's right of a set-off." (Pet. A.24).

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[9] Indeed, *Massey* relied upon so heavily by the bank provides an excellent illustration of how properly to evaluate a fact pattern to determine whether the funds were deposited in the ordinary course of business. There the bankrupts, brothers doing business as a partnership, deposited $6225.25 between January 22 and January 25, into their regular business account. Subsequent to the deposits aforementioned but prior to being adjudicated bankrupt on January 27, the depositors wrote a check on their account which the bank honored. The Court of Appeals found that the deposits were made in the usual course of business. In holding that there had been no transfer, but only an ongoing traditional debtor-creditor relationship, this Court carefully noted:

> ". . . there is nothing in the finding to show that the deposit created other than the ordinary relation between the bank and its depositor. The check of the depositor was honored after this deposit [of $6225.25] was made, and for aught that ap-

The bank's contention that only where it is implicated may there be a transfer is unsound, pursuant to the Bankruptcy Act itself, as it confuses the requirements of §§ 60(a) and 60(b) of the Act. The matter is fully explained by the Court of Appeals below, in footnote 9 of its opinion, and need not be repeated here (Pet. A.12).

The rule stated in *Cusick* and in *Mayo* which those courts drew from *Studley* and *Massey*, finds support in the other courts which have had occasion to consider the issue. In *Hood v. Brownlee*, 62 F.2d 675 (4th Cir., 1933), the Court stated:

> "If the bankrupt himself had made the deposit with a view of giving the bank a preferential payment on its claim, the bank would not have had the right of set-off."

The disjunctive "or" was carefully used to distinguish between the intent of the depositor and the intent of the bank in *Joseph F. Hughes & Company v. Machen*, 164 F.2d 983, (4th Cir., 1947), cert. denied 333 U.S. 881. There, in the course of affirming a compromise between the Trustee and several creditors, the Court stated the rule:

> pears Stege Brothers [the bankrupts] might have required the amount of the entire account without objection from the bank, notwithstanding their financial condition."

The factors upon which this court relied in *Massey*, were the identical variables to which the Second Circuit looked in deciding this case. But here those factors presented a very different picture. In *Massey*, the Court looked at the nature of the account itself (which was the bankrupt's regular business account), the fact that a check was actually written by the bankrupts and honored by the bank after the deposits in question had been made, and the nature of the on-going relationship between the bank and the depositor. Here, instead of an ordinary business account, the account was maintained as security for a large loan, and indeed, the account was not even opened until the loan was made; size of deposits in the account were related not to the bankrupts' daily business needs, but rather were a "compensating balance", reflective of the obligation the bankrupt had to the bank. While here no checks were written, it is likely that had they been drafted they would have been dishonored during the final days before set-off.

> "Of course the application of these principles presupposes that there has been a bona fide deposit made in due course of business. *Thus where there has been a deliberate building up of an account for the purpose of enabling the bank to obtain a preference, or* where the deposit is accepted by the bank with the intent of applying it to the depositor's obligations rather than subjecting it to his power of withdrawal, an attempt on the part of the bank to set off the deposit will result in a preference as long as the other conditions of Section 60 are satisfied. *Rector v. Commercial National Bank*, 200 U.S. 420, 26 S.Ct. 294, 50 L.Ed. 533; *Mechanics' & Metals National Bank v. Ernst*, 231 U.S. 60, 34 S.Ct. 22, 58 L.Ed. 121; *Goldstein v. Franklin Square National Bank*, 2 Cir., 107 F.2d 393; *Twentieth Street Bank v. Gilmore*, 4 Cir., 71 F.2d 594; *Callaway v. West Palm Beach Atlantic National Bank*, 5 Cir., 69 F.2d 224, 225; *Frankford Trust Co. v. Comber*, 3 Cir., 68 F.2d 471; *Rupp v. Commerce Guardian Trust & Savings Bank*, 6 Cir., 32 F.2d 234. This result is reached because the apparent deposit is in fact a payment to the bank and the bankruptcy court will look through form to substance and treat the deposit as a transfer of property for or on account of an antecedent debt. *Mechanics' & Metals National Bank v. Ernst*, 231 U.S. 60, 34 S.Ct. 22, 58 L.Ed. 121; *Frankfort Trust Co. v. Comber*, 3 Cir., 68 F.2d 471; *Matters v. Manufacturers' Trust Co.*, 2 Cir. 54 F.2d 1010." 164 F.2d 987, 988. Cert. denied 333 U.S. 881. (Emphasis supplied.)

The same rule was stated in *Citizens National Bank of Gastonia v. Lineberger*, 45 F.2d 522 (4th Cir., 1930); *Bank of Commerce & Trusts v. Hatcher*, 50 F.2d 719 (4th Cir., 1931); *Blue v. Herkimer National Bank*, 30 F.2d 256 (2d Cir., 1929); *Goldstein v. Franklin Square National Bank*, 107 F.2d 393 (2d Cir., 1939); *Frankford Trust Co. v. Comber*, 68 F.2d 471 (3d Cir., 1933); *In re Almond-Jones Co.*, 13 F.2d 152, 157 (1926),

affirmed sub. nom. *Union Trust Co. v. Peck*, 16 F.2d 986 (4th Cir., 1927).[10]

The holding of the majority below conforms fully to the holdings of both this Court and the holdings of the Courts of Appeal which have had occasion to consider the question. None of the circumstances enumerated in Supreme Court Rule 19 are present. The writ should therefore be denied.

III

The Decision Below Fully Complies With the Proper Standards for Review of Summary Judgment Proceedings.

The bank's final argument, respecting the showing necessary to defeat a Motion for Summary Judgment, is nothing more than creation of a straw man and a demonstration to this Court that it can blow him down.

While Glen Head correctly quotes the Court of Appeals in its several references to the Trustee's "allegations," it attempts to mislead this Court by suggesting that the Court's references to "allegations" were to allegations from the Trustee's pleadings

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[10] The bank's reliance upon *Farmer's Bank of Clinton, Missouri v. Julian*, 383 F.2d 314 (8th Cir., 1967) is misplaced. The Court of Appeals properly distinguished that case as having involved a long-standing active account in which withdrawals and deposits were made every day, and having presented no evidence of either the bank or depositor acting rather than in the ordinary course of business. The decision of the referee that the deposits were made by "pre-arrangement" was reversed as being contrary to the evidence. Likewise, *Plymouth County Trust Co. v. MacDonald*, 60 F.2d 94 (1st Cir., 1932) provides no comfort for defendant. There the bank was the one with which the bankrupt conducted all of its routine business, and the deposits were made subject to check. Even the depositor did not intend a transfer. Yet as to a substantial portion of the deposits there, even though the bankrupt had not intended a transfer, the court found one because of the bank's intent in accepting the deposits. No collusion between the parties was deemed necessary.

(Petition, p. 26). But the "allegations" referred to by the Court of Appeals are all, and without exception, inferences premised upon specific facts specifically proven by the Trustee in his answering papers to the Bank's Motion for Summary Judgment. Those facts are set forth in detail in respondent Trustee's statement of the case above.

An example will suffice to show that the Trustee's "allegations" are all firmly rooted in the record which the Second Circuit had before it on review.

All of the Trustee's "allegations" respecting Famighetti's knowledge of Oakland's financial plight were drawn from Famighetti's own deposition. For example, Famighetti testified respecting his knowledge of Oakland's continuing losses.

> Q. When were you first aware, if at all, of Oakland's adverse financial condition, if you were ever aware of it?
>
> A. Well, just as the statements were coming in, there was a loss history. So I felt that they were always in——
>
> Q. In adverse condition?
>
> A. Yes.

Elsewhere in the deposition, Famighetti testified as follows, respecting a bank memo of June, 1970, a year before the set-off:

> Q. Referring to Plaintiff's Exhibit 19, there is reference to the defendant being aware that Mr. Brede was not in a position to pay off the debt in mid-1970.
>
> Do you see that on the first page?
>
> A. In the front?
>
> Q. Right. The first line.
>
> A. Was not in a position to——

Q. It says, "As expected." Was that expectation based upon an oral conversation which you had with Mr. Brede prior to that time or just based upon the financial statements that you had received up to that time or both?

A. It was based on my opinion from the experience with the loan.

Q. Well, what facts was your opinion based upon other than the financial statements sent to you by Oakland since the inception of the loan and the trucking strike that you referred to?

A. Yes, well, from what I could see.

Q. Well, what did you see?

A. From the fact that it was a continuously loss operation, could hardly expect that he would make a substantial payment.

Q. Unless he went to someone else——

A. Some other source.

Q. Were you advised that he was attempting to obtain monies from another source in order to repay the instant loan?

A. I was not aware of it, no.

Q. Now, on the back of that memorandum, there is a reference here to the "bank want(ing) out", with the brackets around the "i-n-g".

Are those the words that the bank said to Mr. Brede?

A. I don't—these would have been my words and I don't believe I used exactly those words.

It is an expression, let's say, within the industry "We want out." And this is essentially——

Q. Well, the words are in quotations and I take it they are in quotations because of the vernacular as opposed to what was actually said.

A. I would have implied as much.

Q. Have you stated the reason why the bank wanted out this morning and in your prior deposition, would you have stated additional reasons at or about the time you made this memorandum?

A. I think I stated earlier in the sense that we expected our time loan to have been paid out at maturity, its anniversary. That did not occur, of course.

Similar evidence in support of all of the Trustee's other factual "allegations" made in the Statement of the Case above respecting the bank's knowledge and its communications with Brede may be found in the record. Only by closing its eyes to the record is Petitioner able to argue the absence of evidentiary support for the Court of Appeals' decision. Insofar as the bank takes issue with the weight and strength of some of the evidence, those arguments are inapplicable in summary judgment proceedings.[11]

The bank next cites cases which hold that an affidavit of counsel not made upon personal knowledge, will not defeat a

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[11] In ruling on a Motion for Summary Judgment, the Court must construe all matters in favor of the opponent of the Motion, and all favorable inferences which can be drawn from his papers should be so drawn. *Adickes v. S. H. Kress Co.*, 398 U.S. 144 (1970); *U. S. v. Diebold, Inc.*, 369 U.S. 654, 655 (1962). Further, facts asserted by the opponent of the Motion are regarded as true. *First National Bank of Cincinnati v. Pepper*, 454 F.2d 626 (2d Cir., 1972). And where the issue at bar is the credibility of one interested witness such as Famighetti, the case must be tried. *The Conqueror*, 166 U.S. 110; *Sonnentheid v. Christian Moerkin Brewing Co.*, 172 U.S. 401. Wright and Miller, Federal Practice and Procedure, §2727, pp. 530-531. The Affidavit of the Trustee's counsel alone was sufficient to create a jury question as to credibility, *Sartor v. Arkansas Natural Gas Corp.*, 321 U.S. 620 (1944). And here far more evidence than just the affidavit was tendered.

Motion for Summary Judgment. The Trustee agrees. But the affidavit of counsel submitted in this cause *was* made upon personal knowledge, and an affidavit of counsel based upon personal knowledge is proper under F.R.Civ. P. 56(e). Wright and Miller, Federal Practice and Procedure, § 2738, p. 699; Moore's Federal Practice, § 56.22(1), p. 56-1320-21; *Stephens v. Brown & Root, Inc.*, 338 F. Supp. 680, affirmed 455 F.2d 1383 (5th Cir., 1972); *Douglas v. Beneficial Finance Co.*, 334 F. Supp. 1166 (D.C. Alaska, 1971) reversed on other grounds 469 F. 2d 453 (9th Circ., 1972).

Contrary to the argument of Glen Head, the Second Circuit has not engrafted an exception to the Federal Rules of Civil Procedure. Your Respondent, the Trustee, responded to the bank's Motion for Summary Judgment with substantial, powerful evidence. The Second Circuit held the Trustee entitled to his day in court because he produced probative evidence which defeated that motion. No new standard has been stated for Summary Judgment proceedings in Trustees' suits. The Court merely applied the well known standards for review of Summary Judgment proceedings to the facts before it. It is only by disregarding those facts that Glen Head is able to argue that the Court of Appeals erred.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

DAVID J. LETVIN
412 Missouri Avenue
East St. Louis, Illinois 62201
(618) 274-0434
Attorney for Respondent

JOEL A. KUNIN
COHN, CARR, KOREIN, KUNIN
& BRENNAN
East St. Louis, Illinois

MURRAY S. LUBITZ
KAZLOW & KAZLOW
Scarsdale, New York
Of Counsel